



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Attn: Mandatory Review, MC 4920 DAL
1100 Commerce St.
Dallas, TX 75242**

501.07-00

Date: April 13, 2012

Number: 201240027

Release Date: 10/5/2012

**ORG
ADDRESS**

Employer Identification Number:

Person to Contact/ID Number:

Contact Numbers:

Voice

Fax

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear :

In a determination letter dated August 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code (the Code).

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. Accordingly, your exemption from Federal income tax is revoked effective October 1, 20XX. This is a final adverse determination letter with regard to your status under section 501(c)(7) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On February 2, 20XX you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code.

You are required to file Form 1120 U. S. Corporation Income Tax Return. You have filed Form 1120 U. S. Corporation Income Tax Return for the years ended September 30, 20XX, September 30, 20XX and September 30, 20XX with us. In addition, for future periods, you are required to file Form 1120 with the appropriate service center indicated in the instructions for the return.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see

that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Internal Revenue Service
Exempt Organizations: Examinations
1100 Commerce Street
MS:4957:DAL
Dallas, TX 75242-1100

Tax Exempt and Government Entities Division

Date: November 17, 2011

ORG
ADDRESS

Taxpayer Identification Number:
Form:
Tax Year(s) Ended:
Person to Contact/ID Number:
ID Number:
Contact Numbers:
Telephone:
Fax:

Certified Mail-Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018-A, *Consent to Proposed Adverse Action*. We will then send you a final letter revoking your exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become

Fax: 214-413-5492final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018-A
Report of Examination
Envelope

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended September 30, 20XX September 30, 20XX

LEGEND

ORG - Organization name XX - Date State - state CO-1 - 1st COMPANY

ISSUE:

Whether ORG continues to qualify for tax exempt status under Section 501 (c) (7) of the Internal Revenue Code of 19XX?

FACTS:

ORG was organized as a "non-profit corporation as approved by the Secretary of State, State of State, as set in the Articles of Incorporation filed with the Secretary of State November 15, 19XX." The corporation is made up of several classes of membership. The Articles of Incorporation also states that "the purposes for which the corporation is organized are: To provide social, fraternal and athletic facilities within the purview and meaning of Article 2.01 (A) of the State Non Profit Corporation Act including but not limited to the establishment and maintenance of facilities for fishing, hunting, swimming, boating, golf, tennis, club house facilities to accommodate social activities of the membership hereof; to protect, preserve and propagate fish and game; to purchase and own such lands and bodies of water as may be desirable in connection therewith; to erect suitable improvements thereon; as well as any other purposes normally incidental to and consistent with the normal operation of a private country club. "

Article Eight (8): "Membership in said corporation, and the classes thereof, shall be as authorized under the By-Laws of said corporation as the same may be from time to time promulgated by the board of directors acting under proper delegation of authority from a majority vote of the then voting membership. "

Article I, Section 1 of the By-Laws, states: "The ORGs affairs are managed by a Board of Directors. Article II of the By-Laws states: "The Board is comprised of nine (9) members, who are Class A members and active members in good standing, elected by ballot at the annual Class A membership meeting to serve terms of three (3) years."

ORG conducts various activities for the pleasure and enjoyment of their members, but is now open to the public. There are still some amenities afforded to members only such as, fishing, swimming, voting, and use of the lake. ORG distributes a newsletter with monthly club news, names of the current board, monthly sales information from the café, restaurant hours, calendar of events, and solicited advertising on the back page. They have opened, and advertise open to the public, because of the decline in membership. ORG had around 450 members in early 20XX, but has only 85 at the present time, thus making it difficult to survive without nonmember income.

ORG has contracted out its kitchen and banquet facilities to CO-1, who books events such as wedding receptions, reunions, and parties. ORG receives the following from CO-1:

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1. 5% of gross sales from the 19th hole or Café
2. 5% of gross sales of food for catered events
3. 25% of gross sales of all alcoholic beverages from bar or catering events
4. In addition, 5% of the gross sales of #1 & #2 will be held by CO-1 to be used only on kitchen repairs, and or upgrades and maintenance of ORG's equipment, including signed for inventory.

ORG operates an 18-hole golf course open to members and the public. The income received by ORG includes membership dues, greens fees, cart rentals, pro shop sales, and a percentage of restaurant & bar sales, and miscellaneous income including interest and rebates received on credit cards.

The exact income attributable to non-members is unknown because ORG did not comply with the record keeping requirements of Revenue Procedure 71-17. Per Revenue Procedure 71-17, without records of non-member sales, all income from cart rentals, restaurant & bar, and pro-shop sales can be assumed to be from nonmembers. However, ORG and agent agreed on a method to determine a reasonable nonmember percentage.

As a result, the analysis of nonmember percentage based on a two year period is noted below:

Year/Period Ended	% of Gross Receipts from nonmember use		Total % Investment nonmember income
September, 20XX	28.3%	(Exhibit A)	28.3%
September, 20XX	27%	(Exhibit B)	27%

LAW:

Internal Revenue Code section 501(c) (7) exempts from federal income tax those organizations or clubs "organized for pleasure, recreation, and other nonprofitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings of which inures to the benefit of any private shareholder."

Section 1.501(c) (7)-1 of the Income Tax Regulations provides that, in general, the exemption extends to social and recreation clubs supported solely by membership fees, dues, and assessments. However, a club which engages in a business, such as making its social and recreational facilities available to the general public is not organized and operated exclusively for pleasure, recreation and other nonprofitable purposes.

Also, Public Law 94-568 was intended to permit organizations to receive up to 15% of its gross receipts from the use of a social club's facilities or services by the general public without jeopardizing its exempt status. Gross receipts are defined for this purpose as those receipts

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from normal and usual activities of ORG including charges, admissions, membership fees, dues, assessments, and investment income, dividends and rents.

Furthermore, Revenue Ruling 68-638 states that a country club that annually host a golf tournament to which the general public is admitted for a charge and uses the net income thereof for club purposes does not qualify for exemption under section 501(c)(7) of the Internal Revenue Code. Revenue Ruling 69-219 states a social club that regularly holds its golf course open to the general public, charging established green fees that are used for maintenance and improvement of club facilities, is not exempt under section 501(c)(7) of the Code. Revenue Ruling 58-589 states solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that ORG is engaging in business and is not being operated exclusively for pleasure, recreation or social purposes. And finally, Revenue Ruling 60-325 states a social club which has been granted exemption from Federal income tax under section 501(c) (7) of the Internal Revenue Code of 1954 may lose its exemption if it makes its club facilities available to the general public on a regular, recurring basis since it may then no longer be considered to be organized and operated exclusively for its exempt purpose.

Revenue Procedure 71-17 sets forth guidelines for determining the effect of gross receipts derived from nonmember use of a social club's facilities on exemption under Internal Revenue Code Section 501 (c) (7) and recordkeeping requirements. Failure to maintain such records or make them available to the Service for examination will preclude use of the minimum gross receipts standard and audit assumptions set forth in this Revenue Procedure.

TAXPAYERS POSITION:

The organization agreed with the IRS Position and will submit Forms 1120.

IRS POSITION:

Based on the examination, the Organization does not qualify for exemption as a social club described in IRC 501 (c) (7). An Organization exempt from federal income taxes as described in IRC section 501 (c) (7) must meet the gross receipts test in order to maintain its exemption. In order to meet the gross receipts test, an organization can receive up to thirty-five percent (35%) of its gross receipts, including investment income, from sources outside its membership without losing its tax exempt status. Within this 35% amount, not more than fifteen (15%) of the gross receipts should be derived from the use of the social club's facilities or services by nonmembers.

The Organization has exceeded the 15% gross receipts standard for nonmember income on a continuous basis for at least two (2) years. ORG received a large percentage of gross nonmember income 28.3% for the period ended September 30, 20XX, and 27% for the period ended September 30, 20XX, which exceeds the limitation of 15% as set forth by IRC 501 (c) (7). Nonmember income is received from the cart rentals, restaurant and bar sales, and pro

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shop sales, but the exact amount of income from these activities is indeterminable because they did not comply with the record keeping requirements of Revenue Procedure 71-17. ORG is advertising it is open to the public and has many amenities to offer residents in the area. The facts of the case show that it is operating in a manner consistent with a for-profit business.

CONCLUSION:

As a result of our examination of your Form 990 for the periods ending September 30, 20XX, and September 30, 20XX, we have determined that your Organization no longer qualifies as an exempt social and recreational club described in IRC 501 (c) (7). Therefore, we are proposing revocation of your exempt status under IRC Section 501 (c) (7) effective October 1, 20XX.

As a taxable entity, you are required to file Form 1120, U.S. Corporation Income Tax Return for the periods open, September 30, 20XX through September 30, 20XX, and subsequent years.